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IN THE

Supreme Court of the United States

OCTOBER TERM, 1996

KOCH FUELS, INC.,
Petitioner,

v.

R. GARY CLARK, in his capacity as Tax Administrator for the State of Rhode Island,
Respondent.

On Petition for a Writ of Certiorari to the Supreme Court of Rhode Island

BRIEF OF COMMITTEE ON STATE TAXATION AS *AMICUS CURIAE* IN SUPPORT OF THE PETITION

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BRIEF OF COMMITTEE ON STATE TAXATION AS *AMICUS CURIAE* IN SUPPORT OF THE PETITION

INTRODUCTORY STATEMENT

This brief is submitted by the Committee On State Taxation as *amicus curiae* in support of the petitioner in the above-captioned matter. Written consent of the petitioner and respondent have been obtained and filed with the Clerk of the Court.

INTEREST OF *AMICUS CURIAE*

The Committee On State Taxation ("COST") is a non-profit trade association that was organized in 1969 as an advisory committee to the Council of State Chambers of Commerce. COST, which separately incorporated on December 11, 1991, has a membership of over 430 major multistate corporations, engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities.

COST's membership includes most of the "petroleum companies" conducting business in the United States. In addition to those targeted companies, many of COST's members are engaged in interstate sales transactions involving Rhode Island customers. The resolution of this controversy is of particular interest to all such companies. However, regardless of whether these companies are arguably subject to the taxing jurisdiction of the respondent as individual entities, the entire membership of COST has a vital interest in ensuring that the mandates of this Court are observed by every court in every State of the union. The clearest such mandate in the state tax context is the Commerce Clause "bright line" physical presence nexus test that this Court enunciated and applied in *Quill Corporation v. North Dakota*, 504 U.S. 298 (1992). While other nexus-related questions continue to challenge state tax administrators and practitioners, this Court made clear beyond cavil one proposition; *i.e.*, absent the actual physical presence of a remote seller of goods within a State, that State cannot assert any sales or use tax burden against the remote seller.

Yet Rhode Island here *deems* physical presence to exist where in fact no such presence can be demonstrated, in order to justify the imposition of a direct tax on a remote seller. Such a nexus theory can also be employed in order to impose the administrative burden of collecting and remitting a use tax imposed on the seller's in-state customer. COST's membership must fear that the literally unruly attitude demonstrated in this instance will pervade the State courts' jurisprudence in *all* nexus controversies.

Furthermore, if Rhode Island courts are permitted to disregard the supreme authority of this Court, what State will hesitate to do so in the future, particularly where the temptation is to craft holdings that yield unlawfully obtained but much-needed tax revenues? Therefore, COST has an interest in this case.

SUMMARY OF ARGUMENT

The Rhode Island Supreme Court's willful disregard of the Commerce Clause "bright-line," physical presence test demands this Court's response for two critical reasons. First, the bright line established in *National Bellas Hess, Inc. v. Department of Revenue of Illinois*, 368 U.S. 753 (1967), and reaffirmed in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), is one of the few absolutes in the state tax arena. Where, as here, state courts feel they can ignore bright-line rules of law with impunity, taxpayers have no certainty. Second, the nature of this offense against binding precedent is such that none of this Court's prior holdings in the state tax arena will be safe from the onslaught of state courts eager to craft holdings that yield or retain ill-gotten tax revenues.

ARGUMENT

This should have been an easy case for the state court. First, the law applicable to this case was simple. *Quill* reaffirmed the "clear rule" which "establishes the boundaries of legitimate state authority," *id.* at 314-15, by holding that a state may not impose a tax, or a collection duty, upon a remote seller "whose only connection with customers in the [taxing] State is by common carrier or the United States mail." *National Bellas Hess, Inc. v. Department of Revenue of Ill.*, 386 U.S. 753 (1967). Second, the facts in this case were simple. Petitioner Koch Fuels, a Delaware corporation headquartered in Kansas, was a remote seller engaged in a discrete number of interstate transactions with a Rhode Island customer. In every instance, Koch Fuels shipped the goods it sold to its customer by common carrier. Pet. App. 19. In short, Koch Fuels was not, and never has been, in Rhode Island in any "physical" way. This decision so flouts the "clear rule" that this Court laid down in *Quill* that certiorari should be granted, even

if for no other reason than to remind courts that *Quill* means what it says, and the only road around *Quill* runs through the halls of Congress.

I. THE PRACTICAL EFFECT OF A DEEMED PHYSICAL PRESENCE NEXUS TEST IS THE DESTRUCTION OF ANY CERTAINTY FOR THE INTERSTATE BUSINESS COMMUNITY, AND HENCE THE IMPAIRMENT OF EFFECTIVE COMPLIANCE

The business community is motivated by two principal needs with respect to the structure and operation of state tax schemes:

(1) the need for certainty (*i.e.*, knowing the rules, expectations, and tax consequences that pertain to taxpayers and their transactions); and

(2) the need for a level playing field (*i.e.*, according the same tax treatment to the same or similarly situated taxpayers or transactions).

It is the first of these needs that is at issue in this case, but both find corollaries in constitutional principles that restrict the states' otherwise sovereign taxing powers. The need for reasonable certainty is embodied in both the Due Process and Commerce Clauses. A well-ordered and stable society is founded upon (a) the due provision of notice concerning one's rights and responsibilities, and (b) consistency in the fact and manner of application and enforcement of such rights and responsibilities. *See, e.g., Cline v. Frink Dairy Co.*, 274 U.S. 445, 463 (1927) ("[t]he principle of due process of law requiring reasonable certainty of description in fixing a standard for exacting obedience from a person in advance has application as well in civil as in criminal legislation").

The need for a level playing field also is embodied in the Commerce Clause. In general terms, the Commerce Clause is informed by "structural concerns about the effects of state regulation on the national economy." *Quill*, 504 U.S. at 312. In particular, a state tax will not pass muster unless it is premised

upon "substantial nexus" of the activity being taxed with the State, and the tax does not discriminate against interstate commerce. *Cf. Complete Auto Transit Co. v. Brady*, 430 US. 274, 279 (1977).

When this Court reaffirmed a "bright-line" physical presence nexus test for Commerce Clause purposes in *Quill*, it satisfied taxpayers' need for certainty through "the demarcation of a discrete realm of commercial activity that is free from interstate taxation." *Quill*, 504 U.S. at 315. Whatever else has remained unresolved in the aftermath of *Quill* (*e.g.*, how much actual presence constitutes "substantial" nexus, versus *de minimis* nexus? Does the same "bright-line" Commerce Clause test control income tax nexus determinations?), remote sellers have understood that their *actual physical presence* within a state is the indisputable prerequisite to the imposition of any sales or use tax burden. Some sellers plan to create substantial nexus through their physical presence nexus, some plan to avoid triggering tax compliance burdens through in-state physical presence — but all understand the ramifications of such presence.

However, where a state dissembles about the very fact of a remote seller's physical contacts with that state, the business community's much-needed ability to plan for and to accommodate compliance burdens and tax liabilities evaporates. In the instant case, the Rhode Island Supreme Court flouts this Court's considered re-affirmation of an absolute rule by opining that Petitioner "Koch's activities created *in practical effect* a physical presence within this state." *Koch Fuels, Inc. v. Clark*, 676 A.2d 330, 334 (R.I. 1996) (emphasis added). The only "activities" cited by that Court relate solely to the Petitioner's arrangements with a *common carrier* — in other words, the same type of arrangements that this Court held did *not* establish the physical presence required to impose a state's sales or use on a remote seller. *National Bellas Hess*, 386 U.S. at 758; *Quill*, 504 U.S. at 315.

If this Court permits even one state court to trespass in such a fashion as the Rhode Island Supreme Court has done, both the

established "boundaries of legitimate state authority" and the "benefits of a clear rule," *Quill*, 504 U.S. at 315, will be impossible to safeguard against swift and inexorable erosion by other state courts. The impact of such a reversion on the business community would be crippling. So long as state departments of revenue and state courts elevate parochial revenue concerns over respect for the bright-line pronouncements of this Court, the rules designed to promote "settled expectations" will devolve into the "quagmire" from which this Court sought to rescue commerce when it reaffirmed the "bright-line" physical presence rule of *National Bellas Hess*. *Quill*, 504 U.S. at 315-16 (internal quotation omitted).

II. STATE COURTS MUST NOT BE PERMITTED TO SNUFF OUT THE "BRIGHT LINE" PHYSICAL PRESENCE NEXUS TEST, IN BLATANT DISREGARD OF THE COURT'S DECISIONS.

The number of petitions for certiorari submitted to this Court each year by state taxpayers challenging the constitutionality of taxing schemes or the application of specific state laws is significant. While many of those petitions request the Court's guidance regarding the proper *extension* of principles the Court has previously enunciated (*e.g.*, to distinct fact patterns or to different types of taxes), it cannot have escaped the attention of this Court that a disturbingly high percentage of petitions currently being filed serve notice that state courts are, particularly in state tax cases, refusing to apply established Supreme Court precedent.

Not only does the Rhode Island Supreme Court's decision significantly imperil the modest levels of certainty and consistency in application of sales and use tax nexus principles that *Quill* introduced, but it also implicates this Court's very mandate to interpret the constitutional restrictions on states' taxing rights. Grumble though they may (and do, frequently and publicly) over the actual holding in and ramifications of *Quill*, state tax administrators and state courts must respect the favored interstate commerce zone that this Court demarcated in *Quill*, just as

taxpayers give deference to the many decisions this Court issues that uphold state taxing schemes. Both the holding and strong message in *Quill*, and indeed the very supremacy of this Court, are thrown into question every time a state court chooses the course that Rhode Island's courts have elected in this case.

CONCLUSION

For the reasons set forth above, the Committee On State Taxation respectfully requests that the Court grant a writ of certiorari and reverse the decision of the Supreme Court of Rhode Island.

Respectfully submitted,

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